

## Update on Probe Monitoring: tariff differentials and consumer switching

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In September of last year, Ofgem introduced new conditions to tackle unjustified tariff differentials into the licences of energy suppliers in Great Britain. These measures addressed directly the widespread overcharging of certain groups of customers that Ofgem identified during its 2008 Energy Supply Probe.

In this paper, we report on the impact of these measures on tariff differentials and consider whether further actions are needed to address any remaining issues. We also present research on recent levels of switching activity.

Overall, Ofgem's actions have been successful in delivering substantial reductions in the tariff differentials identified during the Probe. In the majority of cases, the remaining differentials are now consistent with our understanding of the differences in costs. This has delivered material benefits to the affected consumers, which include an above average proportion of vulnerable groups.

However, the analysis in this paper shows that some individual areas of concern remain and some new issues have emerged, which require further consideration. We take seriously any case in which we believe suppliers have set price differentials in a way which cannot be objectively justified, and we are committed to the protection of all consumers. As a result, and in line with our published Guidelines, we have moved to the first stages of our bespoke enforcement procedure with two suppliers we believe may be in breach of SLC 25A. We have asked these suppliers to provide an objective justification for their pricing policies, where we believe such policies may be leading to a material detriment to a significant proportion of these suppliers' affected customers.

The introduction of the new licence conditions has also seen a notable increase in the use of introductory offers, particularly for customers signing up online. Ofgem permitted such offers under our Guidelines, as we would anticipate such inducements to switch as part of a vibrant competitive market. However, it can lead to the impression of sustained tariff differentials if the temporary nature of these offers is not obvious. It is vital, and a requirement of our Guidelines, that the terms of these deals are marketed transparently to customers.

## Associated Documents

- Electricity and Gas Supply Market Report (73/10), 16 June 2010  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Electricity%20and%20Gas%20Supply%20Market%20Report%20June%202010.pdf>
- Financial Information Reporting: Guidance, 20 October 2009  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Financial%20Information%20Reporting%20Guidance.pdf>
- Implementation of the Energy Supply Probe Retail Markets (126/09), 19 October 2009  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Implementation%20of%20the%20Energy%20Supply%20Probe%20Retail%20Markets.pdf>
- Guidelines on Cost Reflectivity between Payment Methods and the Prohibition of Undue Discrimination in Domestic Gas and Electricity Supply Contracts (102/09), 7 August 2009  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Guidelines%20on%20Cost%20Reflectivity%20and%20Undue%20Discrimination%20in%20Supply.pdf>
- Addressing undue discrimination (72/09), 26 June 2009  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Addressing%20Undue%20Discrimination.pdf>
- Addressing undue discrimination - final proposals (42/09), 15 April 2009  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Addressing%20undue%20discrimination%20-%20final%20proposals.pdf>
- Energy Supply Probe - proposed retail market remedies (41/09), 15 April 2009  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Retail%20package%20-%20decision%20document.pdf>
- Addressing unfair price differentials (01/09), 8 January 2009  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Consultation%20on%20addressing%20unfair%20price%20differentials.pdf>
- Energy Supply Probe - Initial Findings Report (140/08), 6 October 2008  
<http://www.ofgem.gov.uk/Markets/RetMkts/ensuppro/Documents1/Energy%20Supply%20Probe%20-%20Initial%20Findings%20Report.pdf>
- Enforcement guidelines on complaints and investigations (232/07), 28 September 2007  
<http://www.ofgem.gov.uk/ABOUT%20US/ENFORCEMENT/Documents1/Enforcement%20Guidelines%20post%20consultation.pdf>

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## Summary

### Context

In 2008 Ofgem conducted an investigation into the functioning of competition in GB energy retail markets (The Energy Supply Probe). This revealed that while competition was generally effective, there were several important areas for further attention.

One urgent issue was the widespread overcharging of certain groups of consumers (unjustified tariff differentials). This was set against a background of encouraging, yet underdeveloped levels of consumer engagement. These two issues are linked. Consumers' reluctance to switch creates market conditions in which suppliers face lighter competitive constraints on their pricing strategies.

As a result of our findings in the Probe, last year we began to implement a broad package of remedies in the energy retail markets. These measures were designed to address both a wide range of concerns surrounding consumer engagement and more specific issues, such as unjustified tariff differentials.

In this paper we report on changes in tariff differentials, and in particular the impact of two new licence conditions introduced in September 2009 to promote cost reflectivity and prevent undue discrimination between different groups of consumers. We also present research on recent levels of switching activity. This provides a context to our findings on differentials - and also a baseline for the ongoing monitoring of the wider Probe remedies package.

### Our Findings

Overall, our actions have been successful in delivering substantial reductions in the tariff differentials identified during the Probe. In the majority of cases, the remaining differentials are now consistent with our understanding of the differences in costs. This has delivered material benefits to the affected consumers, which include an above average proportion of vulnerable groups.

However, the analysis in this paper shows that some individual areas of concern remain and some new issues have emerged, which require further consideration. If we believe that there is a possibility that the licence conditions have been breached, we will take action by proceeding through the enforcement stages set out in the Guidelines published alongside the new conditions.

Regarding switching, this report suggests switching levels remain high, but have fallen slightly since 2008. Switching in 2009 was 17% for gas customers and 18% for electricity customers, down from 20% in electricity and 19% in gas during 2008. However, it is important to place these figures in the context of the more static pricing strategies seen during 2009. Further, it is encouraging to see evidence that more energy consumers are making good switching decisions: 67% of customers

who switched their electricity account in 2009 believe they have saved money, compared with 62% in 2008.

The key findings in chapter 2 on tariff differentials are presented below:

- Price premiums for customers paying by prepayment meter (PPM) have been completely eliminated and are now, on average, £19 below the equivalent Standard Credit (SC) tariffs. The average premium over direct debit (DD) for a typical dual fuel prepayment meter customer has also fallen from £111 to £69.
- The differential between SC and DD bills has increased by £29 since October 2007. We have raised this increase with suppliers and based on our discussions we understand this to be reflective of the more widespread use of prompt pay discounts and the increased concentration of bad-debt costs onto the non-prompt-paying group. For those customers that pay promptly, SC-DD differentials have fallen to £45.
- We see the introduction of prompt pay discounts as a helpful innovation in the energy retail markets but only if the level of the discount can be objectively justified and if it is marketed and administered in a fair and transparent way. We will take very seriously any cases in which we believe a suppliers' prompt pay discount is causing undue discrimination to their non-prompt paying, standard credit customers.
- We are also monitoring how suppliers market these discounts, and have carried out our own research on customers' reactions to prompt pay through Ofgem's Consumer Panel. We will be publishing a report summarising the results of this research on our website shortly.
- The balance of margins on gas sales, with respect to electricity, has reversed since the Probe. This suggests that the implied cross-subsidisation from electricity revenues to gas has diminished and that the disproportionate detriment to off-gas grid customers, discovered in the Probe, no longer exists.
- Our updated findings on the premiums charged by former electricity incumbents in their former franchise areas show that systematically high, in-area prices have fallen dramatically in most cases. This represents a benefit to a large proportion of "sticky" customers who remain with their ex-incumbent supplier. However, we note the persistence of a small number of anomalies in regional pricing and some remaining "in-area" premiums.
- The most competitive offers remain online, direct debit, dual fuel deals. Our updated analysis has shown that our new licence conditions have not precluded strong competition between small suppliers and the Big 6, who compete by offering attractive initial and fixed price deals. However, we remain concerned that the time-limited nature of these tariffs is not always evident from the marketing material and it is not always clear what happens to prices at the end of the offer period.
- We take seriously any case in which we believe suppliers have set price differentials in a way that cannot be objectively justified and we are committed to

the protection of all consumers. As a result, and in line with our published Guidelines, we have moved to the first stages of our bespoke enforcement procedure with two suppliers we believe may be in breach of SLC 25A. We have asked these suppliers to provide an objective justification for their pricing policies, where we believe such policies may be leading to a material detriment to a significant proportion of these suppliers' affected customers.

The key findings in chapter 3 on consumer switching are presented below:

- The headline survey result indicates that there has been a slight fall in the total incidence of switching. During 2009, 17% of all gas customers surveyed and 18% of all electricity customers surveyed switched their supplier. This compares to 20% and 19% of gas and electricity customers, respectively, during 2008.
- While this represents a fall in the rate of switching, it is important to place these figures in the context of the more static pricing strategies seen during 2009. For example, in 2009 average prices fell only 6%, in contrast to 2008, when average prices rose some 37%.
- Of those who have never switched, the majority (83%) of customers on either fuel are aware that it is possible to switch, but this still leaves 1 in 5 customers who are unaware. This proportion suggests that suppliers could be doing more to inform their customers of switching possibilities.
- It is also encouraging to see evidence that more customers are making good switching decisions. Of those customers who switched to save money, 67% of those who switched electricity supplier and 64% of those who switched gas supplier believe they are now paying less as a result of their switch. This is a statistically significant improvement for electricity, where in 2008, 62% said they believed they were paying less than they would have without switching.

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## 1. Background

### The Energy Supply Probe

1.1. The Energy Supply Probe (hereafter "the Probe") uncovered a number of tariff differentials in the GB energy supply market that appeared to have no cost justification<sup>1</sup>. These included differentials between payment methods, off-gas grid differentials, and differentials on the tariffs charged by the five former electricity incumbents between "in-area" and "out-of-area" customers. Further, we found that vulnerable groups were more prevalent in the market segments affected by these differentials.

1.2. On payment methods, the Probe found that customers who paid for their electricity and gas using standard credit or, to a lesser extent, via a prepayment meter paid significantly more compared to those using direct debit than could be justified by costs. Throughout November to December 2008, shortly after the publication of our Initial Findings Report in October 2008, a number of suppliers changed their standard credit and prepayment meter tariffs. This brought the premium on prepayment meter tariffs in line with the assessment we had made of the cost to serve these customers at the time. This was not the case, however, for standard credit premiums, where even after the price reductions, these tariffs remained substantially above the level justified by our 2008 analysis of costs.

1.3. Similar unjustified premiums were uncovered across tariffs for different fuel types. The Probe found that the five former incumbent electricity suppliers consistently earned higher margins on electricity supply than on gas. These higher margins indicated likely cross-subsidisation at the expense of electricity-only customers, and in particular those unable to take advantage of dual fuel deals.

1.4. Finally, on regional differentials, the Probe found that the five former incumbent electricity suppliers charged electricity customers in their former monopoly regions an average of 10 per cent more than comparable "out-of-area" customers. Price changes that occurred during the time we were undertaking the Probe narrowed this differential to around 6 per cent on average. However, based on data provided to us by suppliers we were unable to find a cost justification for this premium.

1.5. These findings were set against a backdrop of encouraging, but underdeveloped, levels of consumer engagement and switching. We identified a group of 'confident deal seekers' - those who sought the best deals and typically made good switching decisions - who represented a small minority. However, we also uncovered groups of customers who were confused, nervous, not interested in switching, or disengaged<sup>2</sup>. Of particular concern was evidence that vulnerable consumers were less actively engaged in the energy market than others.

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<sup>1</sup> Energy Supply Probe - Initial Findings Report (140/08), 6 October 2008

<sup>2</sup> Results of Ipsos-MORI Ofgem Customer Engagement Survey, July 2008

## Probe remedies and monitoring

### Undue Discrimination

1.6. In efforts to address concerns about unjustified tariff differentials between payment types, regions and between customers on and off the gas grid, Ofgem consulted on a range of measures to address unfair price differentials<sup>3</sup> and subsequently modified the Standard Conditions of the Electricity and Gas Supply Licences (SLCs), introducing, with effect from 1 September 2009:

- SLC 27.2A, requiring that any difference in the terms and conditions offered in respect of different payment methods is cost reflective, and
- On a temporary basis, SLC 25A, prohibiting undue discrimination between terms and conditions offered to different groups of customers.

1.7. Importantly, these new conditions do not remove the ability for firms to offer different terms to different groups of customers. However, they have been designed so that such conduct must be objectively justified. The grounds for objective justification are set out in our Guidelines<sup>4</sup>, and these include cost reflectivity, the provision of an initial offer and supplier innovation.

1.8. The Guidelines also explain our approach to enforcement – including the consideration that we give to materiality and the procedure we will generally follow for any suspected breaches of SLC 25A. This bespoke procedure for SLC 25A is designed to be staged in its escalation, giving weight to the level of consumer detriment arising. If we identify a concern with a pricing differential, either on our own or following a complaint, we will write to the supplier concerned. The staged enforcement process will then generally proceed as follows<sup>5</sup>:

- *Stage 1:* Following the letter, we will allow the supplier the opportunity to respond and provide objective justification for the tariff differential.
- *Stage 2:* If we are not satisfied with the supplier's explanation, we will write to the supplier again to explain why. We will allow the supplier the opportunity to respond again. If, at this stage, the supplier revises its pricing structure to satisfy Ofgem's concerns, we are unlikely to take further action.
- *Stage 3:* If we remain unsatisfied, we will expect the differential to be reversed. If this is not the case, we will make the case for a licence breach in line with the existing Enforcement guidelines<sup>6</sup>.

1.9. As discussed above we have already moved to Stage 1 with those suppliers we believe may be in breach of SLC 25A.

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<sup>3</sup> Addressing Unfair Price Differentials (01/09), 8 January 2009

<sup>4</sup> Guidelines on Cost Reflectivity between Payment Methods and the Prohibition of Undue Discrimination in Domestic Gas and Electricity Supply Contracts (102/09), 7 August 2009 (hereafter the "Guidelines")

<sup>5</sup> See Guidelines, Ref 102/09 p.19

<sup>6</sup> Enforcement guidelines on complaints and investigations (232/07), 28 September 2007

## **Consumer Behaviour**

1.10. In addition to the licence conditions tackling undue discrimination, we have also introduced additional remedies following the Probe that include a package of licence conditions to encourage consumer engagement with the energy retail market and to help consumers find and switch to the best deal that suits them<sup>7</sup>.

1.11. In particular, a new licence condition on the provision of information in bills should improve customers' ability to compare tariffs and engage in the market effectively. We have also made substantial additions to the licence condition surrounding the marketing of energy by suppliers. These include obligations on suppliers to provide customers with a written estimate of the annual charge of a new contract prior to completing a sale. We expect that these additions should improve customers' ability to make well-informed choices when choosing their energy supplier and should help build consumer confidence in the competitive market.

## **Monitoring**

1.12. As part of our commitment to expand and deepen our market monitoring, we have included a new licence condition to mandate the major vertically-integrated supply companies to publish annually detailed financial information on their profits, underlying costs and revenues<sup>8</sup>. This information will be requested on a separated accounts basis across their gas supply, electricity supply and electricity generation businesses. This will improve our understanding of the profitability of the separate profit centres within vertically integrated entities, giving us a clearer picture of how different pricing policies impact profits, not only across the whole business, but also within them.

1.13. Furthermore, from April 2010 we have started to collect information on total domestic customer numbers and total switching by fuel type and region. We have also begun collecting data regularly on customer numbers, switching and objections to transfer in the non-domestic market.

1.14. Ofgem has committed itself to a thorough review of the impact of the measures introduced as a result of the Probe before SLC 25A terminates at the end of July 2012. For the avoidance of doubt, this report does not constitute a component of this review. Rather, it presents our ongoing analysis of the energy retail markets.

## **Standards of Conduct**

1.15. In addition to the package of licence conditions in 2009, we also introduced overarching Standards of Conduct ("the Standards") which set out our expectations of suppliers' behaviour when dealing with domestic and small business customers<sup>9</sup>.

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<sup>7</sup> Implementation of the Energy Supply Probe Retail Markets (126/09), 19 October 2009

<sup>8</sup> Financial Information Reporting: Guidance, 20 October 2009

<sup>9</sup> Standards of Conduct for suppliers in the retail energy market (127/09), 19 October 2009

These include guidelines on the appropriate conduct of suppliers during and after the sale of a new product and when dealing with customers if a mistake is made or if a customer chooses to switch its energy supplier. We subsequently met with all major suppliers to set out our expectations and to understand how the Standards are being adopted.

1.16. We are committed to monitoring suppliers' adherence to the Standards and the impact they have had on consumers' experience. We are monitoring this through a variety of means, including: the collection of customer survey data; further work with our Consumer Panel; ongoing monitoring of suppliers' marketing materials and offerings on switching sites<sup>10</sup>. The extended monthly data that we are collecting from suppliers will also help us understand the impacts of the Standards insofar as they help us to monitor the effectiveness of customer switching decisions. Furthermore, we also intend to publish examples of good and bad practice in relation to the Standards of Conduct.

1.17. As well as publishing examples of good and bad practice in relation to the Standards of Conduct, we will take suppliers' adherence to them into account when deciding whether:

- it is appropriate to conduct an investigation in respect of a potential breach of a distinct, but related, licence condition; and
- to take other regulatory measures to address any relevant concerns, e.g. proposals to modify licence conditions.

### **Further comments**

1.18. Since the Probe, our analysis has been widely used by a broad range of industry stakeholders, consumer interest groups and the media. In some cases, the figures and analysis presented in the Probe have been misinterpreted.

1.19. For example, the analysis presented in the Probe on the differences between the costs suppliers' incur when providing different payment methods was not a recommendation for the appropriate premium or discount suppliers should charge. Rather, the use of suppliers' cost data was intended to inform the analysis on tariff cost reflectivity, where the cost data could be used to justify certain tariff differentials. This also applied to the calculations of the differences between the costs underlying electricity and gas tariffs and between "in-area" and "out-of-area" tariffs. Ofgem recognises that the costs of supply to different consumer groups will vary over time and by supplier.

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<sup>10</sup> We note the close links here with Consumer Focus' work examining the scope for improvements to the Confidence Code.

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## 2. Update on Tariff Differentials

This chapter updates our Probe analysis on differentials between payment methods, off-gas grid differentials and differentials between the tariffs charged to "in-area" and "out-of-area" customers. It also looks at wider impacts of our remedies on the domestic energy retail market as a whole.

2.1. During 2008-09, we observed suppliers take positive steps to address some of the undue differentials that we identified in the Probe, however, we were concerned about the rate and durability of progress. The introduction of SLCs 27.2A and 25A, in September 2009, has been successful in protecting these positive steps and in many cases delivering further reductions in tariff differentials. In the majority of cases, the remaining differentials are now consistent with our understanding of the differences in costs.

2.2. However, we are aware that some individual areas of concern remain and some new issues have emerged. These developments may have caused material detriment to certain groups of consumers. We are committed to the protection of all consumers and, as a result, and in line with our published Guidelines, we have already moved to Stage 1 of our bespoke enforcement procedure with two suppliers we believe may be in breach of SLC 25A. We have asked these suppliers to provide an objective justification for these pricing differentials, where we believe such differentials may be leading to a material detriment to a significant proportion of these suppliers' affected customers.

2.3. We are also monitoring the wider impact of our remedies on the domestic energy retail markets. This has shown that our remedies have not precluded strong competition between the Big 6 and small suppliers, in those parts of the market where small suppliers offer the lowest price tariffs. However, we remain aware that the marketing by suppliers of time-limited tariffs, used by the Big 6 to compete with small suppliers, has scope for improvements.

2.4. The analysis in this chapter begins with an update on tariff differentials by payment method. In particular, we look at the differences between prepayment meter (PPM), standard credit (SC) and direct debit (DD) annual bills. The figures in this chapter assume constant annual electricity and gas consumption of 3.3MWh and 20.5MWh, respectively<sup>11</sup>.

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<sup>11</sup> The values for electricity and gas demand reflect the 'medium consumption customer' and match the annual demand values used in the Energy Supply Probe. We are aware these values may have changed and will be consulting on updated domestic consumption values later in 2010. The analysis presented in this chapter is up-to-date to the best of our knowledge as of the date of publication. All customer bills have been calculated on a nominal annual basis, using the latest available tariffs. This analysis therefore takes a forward-looking approach, assuming a customer enters into a supply contract today and holds it for 12 months. As suppliers change their tariff offerings, going forward, the charts and tables presented in this report will no longer be valid.

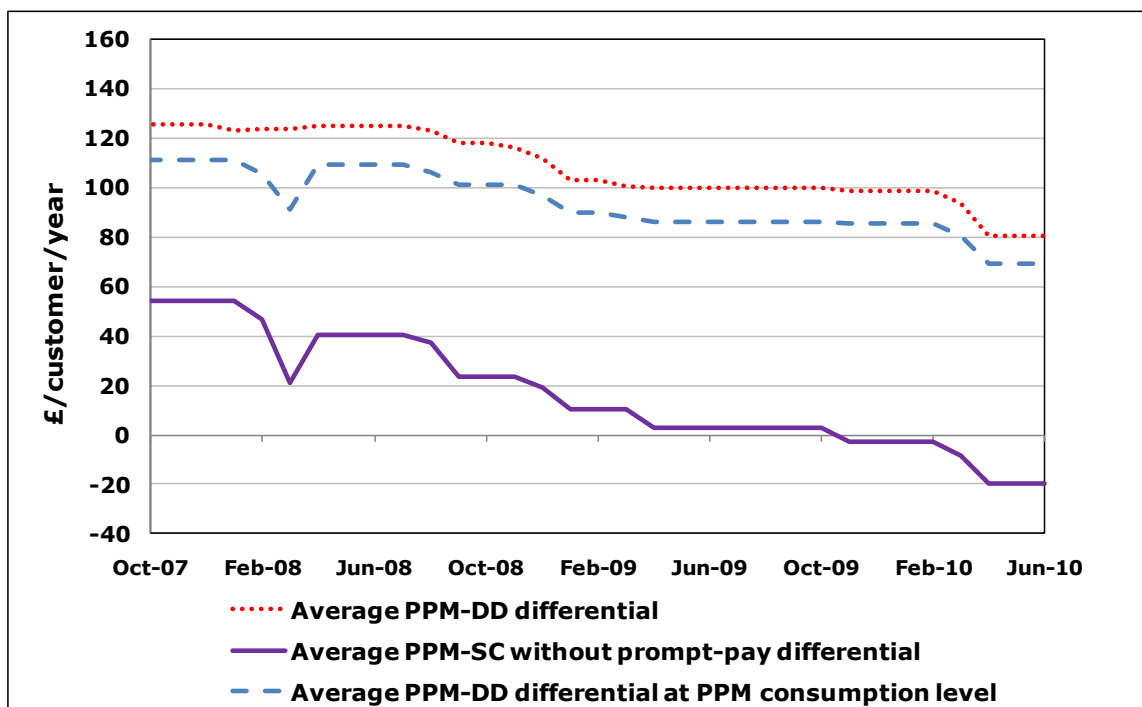
## Prepayment meter premiums

2.5. Since announcing the Probe, the average premium paid by prepayment meter customers compared with both direct debit and standard credit customers has steadily fallen. This can be seen in Figure 2.1 which shows the average differential, across the Big 6, between the annual bills of customers on gas and electricity PPM tariffs with respect to both DD and SC dual fuel tariffs. Since October 2007 the average differential between a PPM and DD bill has fallen from £126 to £81. This differential is lower still, at £69, if the different consumption pattern of an average customer using a prepayment meter is taken into account. In both cases, this differential is now less than the £88 indicative cost difference between the supply costs of a prepayment meter customer with respect to a customer paying by direct debit, identified during the Probe.

2.6. Figure 2.1 also presents the differential, across the Big 6, between the bills for prepayment meter and standard credit customers. The chart shows that this differential has fallen from nearly £55, in October 2007, to a negative premium of £19 today (i.e. PPM tariffs are now, on average, cheaper than SC tariffs without a prompt pay discount). This shift has been driven, to a large extent, by at least one supplier offering a significant discount on PPM tariffs, with respect to SC and a number of other suppliers equalising their PPM and SC tariff offerings.

2.7. The figure also shows that at the last round of price cuts in February and March of this year, suppliers continued to make efforts to improve price differentials, where the combined effect, across all suppliers, were further reductions in the PPM-DD and SC-DD differentials.

**Figure 2.1 Average prepayment meter premiums**



Source: Ofgem analysis

2.8. In summary, Figure 2.1 shows that the introduction of SLCs 27.2A and 25A has been successful in protecting the decline in undue premiums on customers paying by prepayment meter and bringing about further reductions to the benefit of prepayment meter customers. Prepayment meter customers now pay, on average, less than those customers on Standard Credit.

### Standard credit premiums

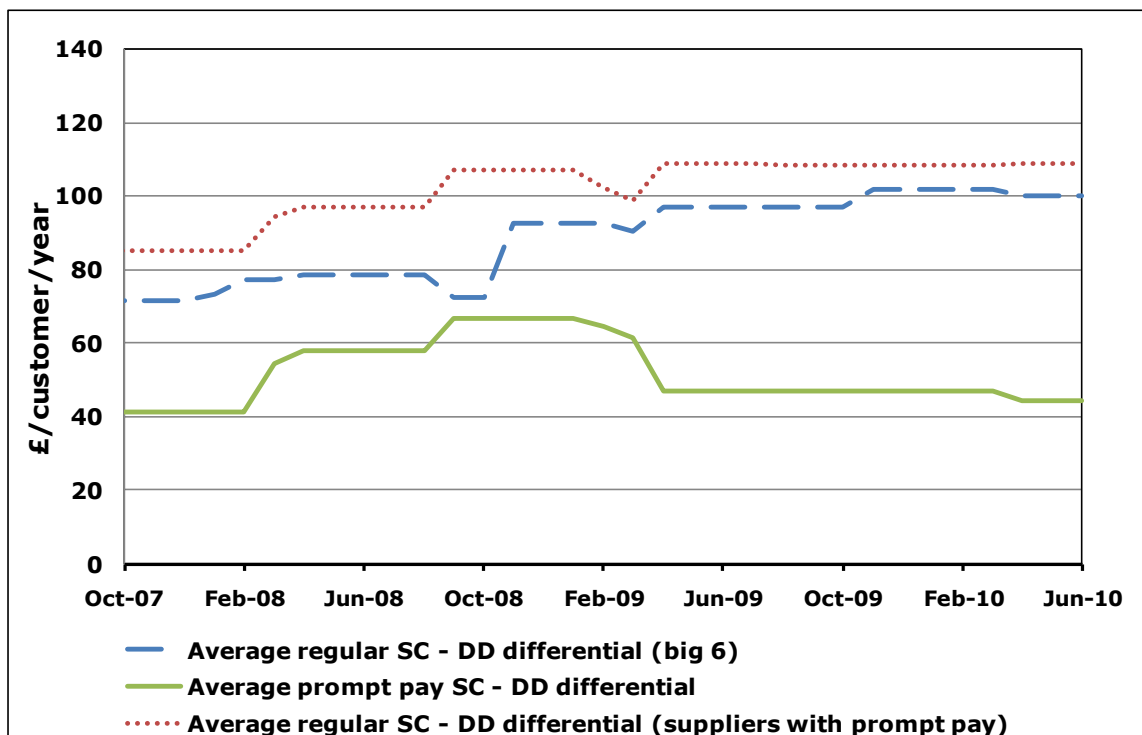
2.9. Figure 2.2 presents the change in the average differential between regular (i.e. non prompt pay) SC bills with respect to DD bills across the Big 6. It indicates a marked increase in the differential between regular SC and DD bills, where this differential has increased by £29, since October 2007, across the Big 6. We note that the latest round of price cuts, earlier this year, have had a small positive effect on the size of this differential, reducing it by 2% since March.

2.10. While we are concerned that the SC-DD differential has increased, we cannot fully assess whether the overall increase in the SC-DD differential is justified. This is because our most recent cost data dates from 2007, some time before the credit crisis and recession. However, we have raised this matter with suppliers and based on our discussions we understand this to be reflective of the increased concentration of bad-debt costs onto the non-prompt-paying group of customers, following greater

introduction of prompt-pay offerings, and the overall upwards trend of bad debt costs during the recession.

2.11. We will continue to monitor this differential closely, and are investigating it further, both from a cost reflectivity perspective and in terms of the wider terms and conditions around prompt pay discounts. Towards this, we will be looking to carry out an update on the costs underlying the different payment methods across the Big 6 energy suppliers.

**Figure 2.2 Average standard credit premiums**



Source: Ofgem analysis

2.12. Figure 2.2 also highlights the savings customers can earn through prompt pay discounts. The introduction and use of prompt pay discounts is discussed in more detail below. In summary, it allows a customer paying by standard credit to earn a discount on his/her quarterly bill if the supplier receives payment within a given time frame. In June 2010, the average size of prompt pay discount, across those suppliers that offered them, was some £61, but this value varies significantly between suppliers (see Figure 2.3).

2.13. We note that the differential between prompt pay SC and DD bills has also slightly increased since October 2007, but has fallen since October 2008 - the date of the Probe Initial Findings Report - and has also fallen further following the February and March price cuts. This may reflect the fact that most suppliers have not chosen

to allocate a large proportion of the increase in costs of bad debt to prompt payers. We are monitoring this differential on an ongoing basis and, as detailed above, we will be looking to update our data on the costs underlying different payment methods.

## Prompt pay discounts

2.14. Prompt pay discounts allow a customer paying by standard credit to earn a discount on his/her quarterly bill if the supplier receives payment within a given time frame. To date, four of the Big 6 suppliers have introduced prompt pay discounts for standard credit customers<sup>12</sup>. Figure 2.3 compares the features of the discounts offered by these suppliers.

**Figure 2.3: Comparison of supplier prompt pay discounts**

Supplier	Size of quarterly discount	Total potential annual saving (dual fuel)	Time frame to earn discount
British Gas	Max £3.75 per quarter (gas) Max £3.75 per quarter (electricity)	£30.00	14 days
E.ON	3% of total bill	£35.60	14 days
ScottishPower	Daily electricity discount of 13.7p Daily gas discount of 27.4p	£150.00	10 days
SSE	2.5% per bill	£29.85	10 days

**Source: Supplier websites**

2.15. Figure 2.3 indicates that the size of prompt pay discounts varies significantly across suppliers, while the time frames to earn the discount do not. Of the suppliers offering prompt discounts, ScottishPower currently offers the largest, amounting to £150 per year for a dual fuel customer paying in-time on all four quarterly bills, with SSE offering the lowest.

2.16. We view the introduction of prompt pay discounts as a helpful innovation in the energy retail markets, since their use improves suppliers' ability to offer cost reflective tariffs to those who pay quickly and are therefore cheaper to serve. However, it is important that the nature of these discounts, and the circumstances under which they are payable, are explained very clearly in customer literature, including sales literature, and we are monitoring how suppliers market these discounts. Prompt pay discounts, including the time frames a customer must pay in order to qualify for the discount, also raise questions regarding the protection of vulnerable customers.

<sup>12</sup> EDF also offers a prompt-pay discount to customers who opt-in to the scheme, but for this reason it has not been included in the prompt-pay analysis in this report.

2.17. We will continue to monitor prompt pay discounts and seek to obtain objective justification for any discount we believe may be causing undue discrimination to a suppliers' non-prompt paying, standard credit customers. We will take very seriously any cases in which we believe undue discrimination is taking place, moving to Stage 1 of our bespoke enforcement procedure for SLC 25A, where appropriate. Further, we have carried out our own research on customers' reactions to prompt pay through Ofgem's Consumer Panel. We will be publishing a report summarising the results of this research on our website shortly.

### **Off-gas grid differentials**

2.18. During the Probe we uncovered unjustified premiums across tariffs for different fuel types. We found that suppliers were earning higher margins from their electricity customers than their gas customers – the negative gas margins observed in our October 2008 report implied cross-subsidisation between the two. This meant that electricity customers who were unable to gain access to the gas grid were paying higher margin electricity prices whilst being unable to benefit from low margin gas prices or lower cost dual fuel offerings. In 2008 this amounted to around 4.3 million cases. The Probe also found that customers off the gas grid were more likely to have never switched and thus remain "in-area". This meant they were also paying an associated "in-area" premium.

2.19. Since the publication of the Probe, we have observed a reversal in the balance of margins on gas sales with respect to electricity. Analysis undertaken for Ofgem's June 2010 Electricity and Gas Supply Market Report indicates that net margins on gas sales are just under double those on electricity<sup>13</sup>. This evidence suggests that the implied cross-subsidisation from electricity revenues to gas has diminished and that the disproportionate detriment to off-gas grid customers no longer exists.

2.20. Since October 2009, customers searching for the best electricity and gas deals could have almost always beaten the best dual fuel offering in almost any region and for all three payment methods. This is a positive reaction by suppliers to SLCs 27.2A and 25A and to price competitively across all fuel types, regions and payment methods. It also represents an improvement for the outcomes of customers unable to access dual fuel tariffs.

### **In vs. out of area and regional differentials**

2.21. The Probe found that the five former incumbent electricity suppliers charged electricity customers in their former monopoly regions an average of 10 per cent more than comparable out-of-area customers. The price changes that occurred during the Probe investigation narrowed this differential to around 6 per cent on average. However, based on data provided by the energy supply companies, we found no cost basis for this premium.

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<sup>13</sup> £55/customer/year net margin for gas compared to £30/customer/year for electricity. See Electricity and Gas Supply Market Report (73/10), 16 June 2010.

2.22. This analysis updates our findings on in vs. out-of-area tariff differentials. Figure 2.4 presents the average differential in £ per customer per year, across the five incumbent suppliers' in-area and out-of-area SC electricity bills. The figure also presents the maximum differential for any one incumbent supplier, at any time, as well as the minimum. The figure shows that since the middle of 2008 the average differential between in-area and out-of-area electricity SC bills has nearly halved, falling from over £30 per customer per year to £18<sup>14</sup>. This change has resulted from electricity suppliers reducing their in-area tariffs towards their out-of-area offerings and therefore represents a benefit to a large proportion of "sticky" customers who remain with their ex-incumbent supplier.

2.23. This average value is skewed by a small number of suppliers continuing to offer systematic premiums in their incumbent regions. Vulnerable customers are disproportionately represented in this group. While we have observed a narrowing in the distribution of in-area premiums offered by suppliers following the introduction of DPCR5 network charges, we remain concerned that some of these differentials cannot be objectively justified and are large enough to lead to a potential material detriment to a large number of consumers.

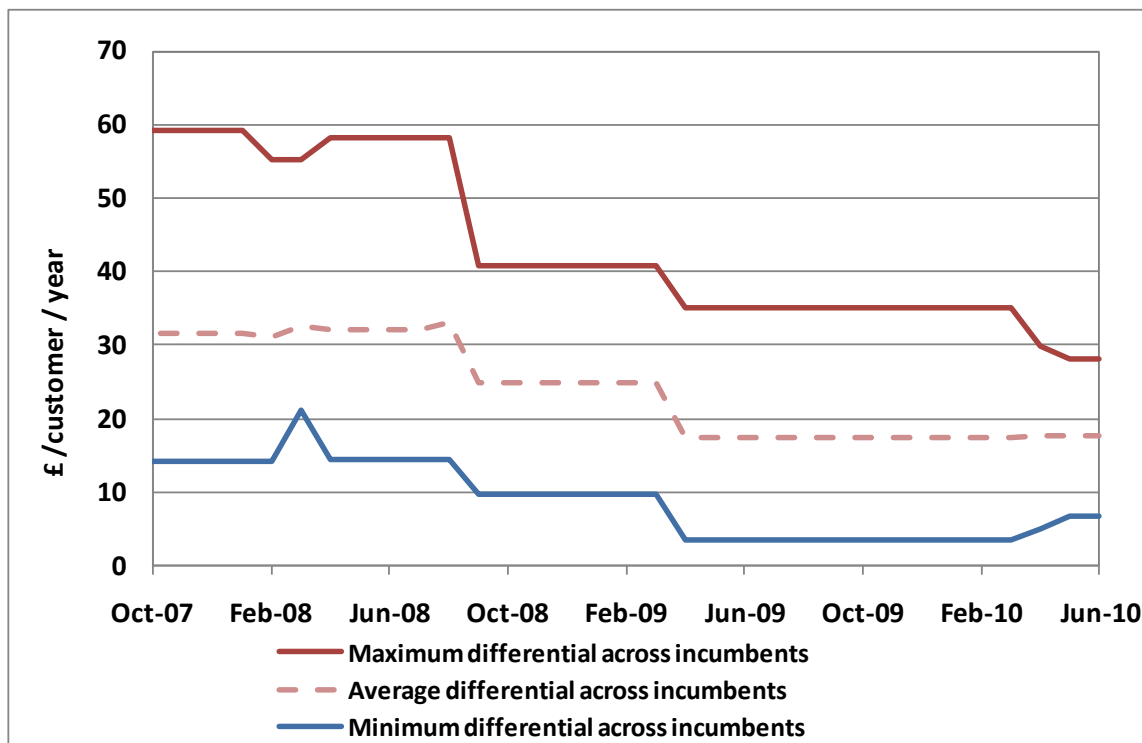
2.24. For these reasons we have moved to Stage 1 of our bespoke enforcement guidelines with those suppliers we believe may be in breach of SLC 25A. We have asked these suppliers to provide an objective justification for these pricing differentials, where we believe such differentials may be leading to a material detriment to a significant proportion of these suppliers' affected customers.

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<sup>14</sup> This value has been calculated based on suppliers' tariffs excluding network charges. The analysis can be repeated to include network charges and results in an average value of £19. This approach, compares suppliers' final prices between regions and is an additional metric we use to assess suppliers' pricing strategies for undue discrimination.

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**Figure 2.4 Average in vs. out-of-area tariff differentials - standard credit**



Source: Ofgem analysis

2.25. In addition to looking at in-area and out-of-area differentials, we are also monitoring regional differentials between suppliers. We undertake this analysis to ascertain whether the differences in tariffs across the country offered by suppliers can be objectively justified. This analysis has highlighted a number of regions in which suppliers have charged significant premiums and discounts compared with their average tariffs. Again we have been engaging with suppliers on these issues, and will proceed through the enforcement stages if we consider that suppliers are failing to address any cases of undue discrimination.

## Wider considerations

### Small suppliers and new entrants

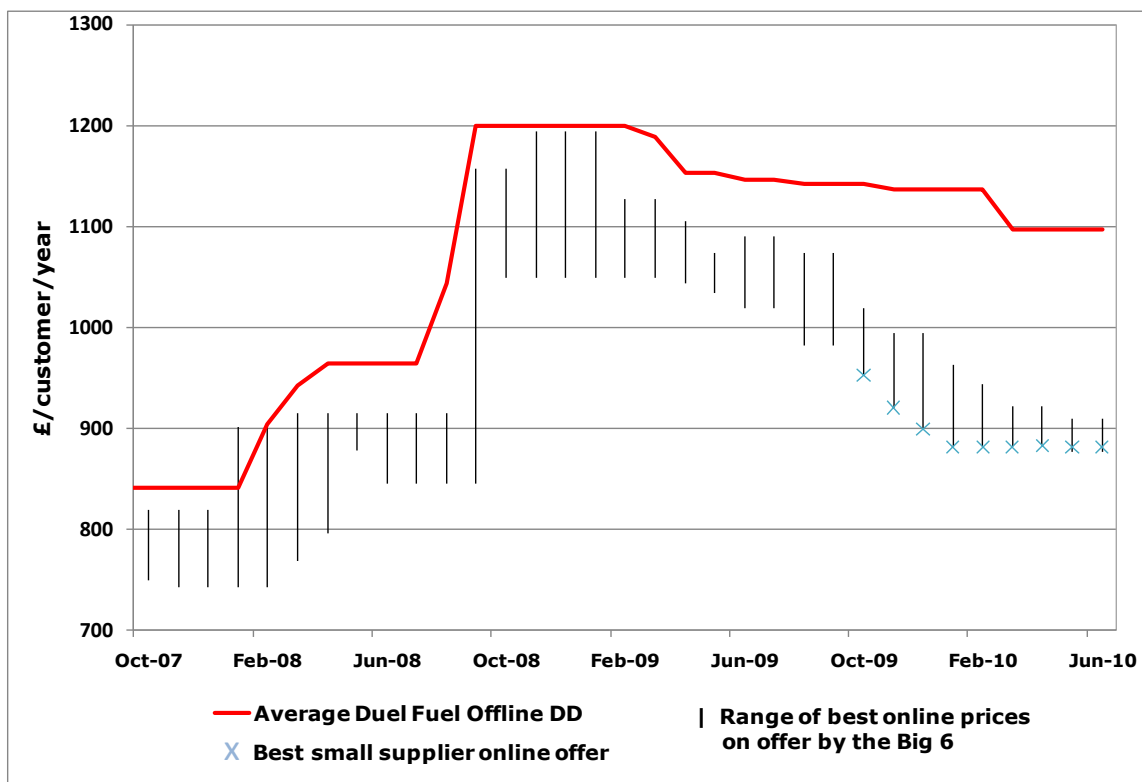
2.26. Alongside monitoring developments within the problem areas we identified at the time of the Probe, we are also monitoring the wider impact of our remedies on the domestic energy retail market as a whole. We are mindful that neither SLC 27.2A nor SLC 25A should reduce competition and innovation in the energy retail market, and that to this end SLC 25A does not remove the ability for firms to offer different terms to different groups of customers. Therefore, we accept that time-limited offers which may be designed to attract new customers; penetrate a market or meet a competitors' offer, are examples of variations which can be objectively justified.

2.27. Our analysis suggests that allowing suppliers to discriminate on justifiable terms has ensured that competition to provide the "best deals" in the market has remained strong to the benefit of those consumers able to access them. Figure 2.5 shows that in the presence of pressure from small suppliers, best offer online bills have decreased throughout 2009-10 and indeed recently, one of the Big 6 has undercut the best small supplier offer.

2.28. In our wider work we are investigating how liquidity in the wholesale market can be improved to enable small suppliers and new entrants to fully compete against the Big 6<sup>15</sup>. In the future, we would therefore hope to see the benefits of greater competitive pressure in a wider cross section of the market, for example, extending to customers who are offline or who cannot pay by direct debit.

2.29. However, our goal is not to eradicate differentials between "best offer" and standard tariffs and the gap observed in figure 2.5 highlights the significant gains which customers can make by switching. Strengthening customers' ability to switch is a key aim of the wider Probe remedies package.

**Figure 2.5 National average dual fuel offline bills vs. best offer online bills**



Source: Ofgem analysis

<sup>15</sup> See Liquidity Proposals for the GB Wholesale Market, Ref 22/10, 22 February 2010

**Time-limited offers: Transparency**

2.30. Currently, the cheapest tariffs used by the Big 6 to compete with small suppliers are either time-limited tariffs or fixed-price offerings. As detailed above, our Guidelines allow suppliers to use such tariffs for the purpose of customer acquisition or to meet competitors' offers and so are not likely to be considered evidence of undue discrimination. However, to qualify under the objective justification on initial offers, the Guidelines require that:

*"a Supplier must specify expressly in advance in their marketing materials that any such price differential or bonus incentive is time limited, and that the said time limited offer will revert, after a reasonable period of time, to the terms and conditions offered to all other consumers"<sup>16</sup>.*

2.31. The updated sales and marketing licence condition (SLC 25) requires information provided in marketing activities to be complete and accurate, and the Standards of Conduct also require suppliers to take all reasonable steps to ensure that customers understand the products that they are being sold.

2.32. We expect suppliers to offer these tariffs in a fully transparent way. For example, time-limited tariffs should be clearly marketed as such<sup>17</sup>. Any promotion of the tariff should ensure that customers are aware that the discount (i.e. from the supplier's standard tariff) will revert after a reasonable period of time. Examples of clear and transparent marketing which satisfy both the Guidelines and the Standards of Conduct would include references to the end date of the discount period and an explanation of what happens next. Furthermore, in accordance with the Standards, how the discount is applied should be clearly set out in a non-confusing manner.

2.33. We currently have concerns that not all online, initial offers are being clearly marketed. We have observed some instances where, we believe, customers could still be uncertain about how long the advertised discount persists and what will happen at the end of the discounted period. Figure 2.6 provides illustrative examples of where we think suppliers could improve the transparency of certain initial offers, and also where key features are currently being made clear.

2.34. We have already discussed our transparency requirements with suppliers and will be closely monitoring tariff marketing on an ongoing basis. Failure by a supplier to adhere to these transparency requirements will lead Ofgem to treat the tariff as an enduring offer and so will require an objective justification for any differential between this and comparable tariffs.

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<sup>16</sup> See Guidelines, Ref 102/09 p.10

<sup>17</sup> See Guidelines, Ref 102/09 p.10

**Figure 2.6 Illustrative examples of online tariff transparency strengths and issues**

Supplier	Tariff	Strength	Issue
EDF	OnlineS@ver 6	<ul style="list-style-type: none"> <li>Online marketing provides clear and accessible information on contract period, exit fees and discounts</li> </ul>	<ul style="list-style-type: none"> <li>Uncertainty about what happens at the end of the fixed period (could be transferred onto a standard tariff or another tariff which is considered 'appropriate')<sup>1</sup></li> </ul>
EON	Fix Online 8	<ul style="list-style-type: none"> <li>Savings referenced on first screen and explained on next</li> <li>Second screen clearly states duration of fixed period and that the offer is limited and early termination fees apply</li> </ul>	<ul style="list-style-type: none"> <li>Online marketing unclear what happens at the end of the contract</li> <li>Terms and conditions difficult to access and unclear what happens at the end of the contract</li> </ul>
British Gas	Websaver 8	<ul style="list-style-type: none"> <li>Online marketing is clear about discounts, fixed contract period, availability and early termination fees</li> <li>Terms &amp; Conditions accessible</li> </ul>	<ul style="list-style-type: none"> <li>Uncertainty about what happens at the end of the fixed period (could be transferred to standard product or to "another product")<sup>2</sup></li> </ul>
Npower	Online 18	<ul style="list-style-type: none"> <li>Terms &amp; Conditions state that the tariff the customer will be placed on at the end of the contract may be more expensive than Sign Online 18</li> <li>Information about the end of the contract is given in Terms &amp; Conditions</li> </ul>	<ul style="list-style-type: none"> <li>Online marketing states savings upfront but fuller information about savings need to be more prominent</li> <li>The link to specific Terms &amp; Conditions could be made more prominent</li> </ul>
SSE	Go Direct 3	<ul style="list-style-type: none"> <li>End date, early termination fees and what happens at the end of the contract are provided on initial product screen</li> </ul>	<ul style="list-style-type: none"> <li>The link to specific Terms &amp; Conditions could be made more prominent</li> </ul>
ScottishPower	Online Energy Reward	<ul style="list-style-type: none"> <li>Fixed period stated upfront</li> <li>Product notes clearly state discounts</li> <li>Early termination fees are presented on the initial product screen</li> </ul>	<ul style="list-style-type: none"> <li>Online marketing and product notes unclear what happens at the end of the contract<sup>3</sup></li> </ul>

Note:<sup>1</sup>The 'appropriate' tariff would always be a discount product. <sup>2</sup>Customers are contacted before being transferred to another tariff in advance of the end of their discount period. <sup>3</sup>Planning to amend for future products.

**Source: Ofgem analysis of suppliers' website and correspondence with suppliers**

### Fixed price tariffs: Availability

2.35. Fixed price tariffs are by their nature only offered on specific terms for a certain period of time<sup>18</sup>. They allow customers who are willing to lock into a contract (e.g. of a years' duration) to pay a fixed unit price for their energy during this time and potentially benefit from a discount and greater certainty regarding their bill value. As set out in our Guidelines, we do not necessarily consider any difference in terms between customers on fixed and standard tariffs to be evidence of undue

<sup>18</sup> See Guidelines, Ref 102/02, p.8

discrimination, provided that the fixed tariff is available to all comparable groups of customers.

2.36. If this was the case, then the price gap between standard and fixed price tariffs would represent a potential gain that customers on standard tariffs could make if they switched. If we observe suppliers are not making fixed price tariffs available to all comparable customers and we consider that this is causing material harm and cannot be otherwise objectively justified<sup>19</sup>, we will take action.

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<sup>19</sup> See Guidelines, Ref 102/02, p.12

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## 3. Update on Consumer Switching

This chapter summaries the headline statistics from a recent omnibus survey measuring switching behaviour during 2009. We carried out similar surveys in 2007 and 2008 and are therefore well placed to track changes in switching behaviour.

3.1. One of the key findings in the Energy Supply Probe was that the GB energy supply markets showed high levels of switching both in comparison to other EU countries and other consumer service sectors. We identified a group of 'confident deal seekers' - those who sought the best deals and typically made good switching decisions - who represented a small minority. However we also uncovered groups of customers who were confused, nervous, not interested in switching, or disengaged<sup>20</sup>. Of particular concern was evidence that vulnerable consumers were less actively engaged in the energy market than others.

3.2. We recognise the importance of active switching behaviour to maintain competitive constraints on suppliers' retail strategies. As a result, we have continued to closely monitor the levels of consumer switching activity. This chapter summarises the headline statistics from a recent omnibus survey measuring switching behaviour during 2009. We will be publishing the full report of the survey on our website shortly.

3.3. The survey was carried out by Ipsos-MORI using a representative sample of GB energy customers who are either solely or jointly responsible for paying the energy bill. The survey was based on interviews with 1,540 electricity customers of whom 1,369 were also gas customers. We carried out similar surveys for 2007 and 2008 and are therefore able to track any changes in switching behaviour. In this year's survey we included questions that put more emphasis on customer's perception of the quality of the switch.

### Key Results

3.4. The headline survey result indicates that there has been a slight fall in the total incidence of switching. During 2009, 17% of all gas customers surveyed and 18% of all electricity customers surveyed switched their supplier. This compares to 20% and 19% of gas and electricity customers, respectively, during 2008. More vulnerable customers such as those aged 65+ and those in socio-economic group E continue to lag behind others in terms of switching rates.

3.5. This small decline in the overall rate of switching should be framed against the pricing activity of suppliers in 2009. During 2009 the degree of pricing activity from the Big 6 was significantly lower than in 2008. For example, in 2009 average prices fell only 6%, in contrast to 2008, when average prices rose some 37%. Lower levels of switching activity are therefore likely to be associated with lower levels of pricing activity, as customers have less of an incentive to search for the most competitive deals.

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<sup>20</sup> Results of Ipsos-MORI Ofgem Customer Engagement Survey, July 2008

3.6. Looking in more detail at the results on those customers who switched, the availability of internet access remains strongly associated with switching rates for both gas and electricity customers. The rate of switching in 2009 was 20% for those with internet access and 10% for those without. However, the popularity of internet only tariffs (that is, accounts managed over the internet) remains low, with just over one in ten customers (12%) taking this option. This is the case, even though around eight out of ten customers have internet access (78% of gas customers; 76% of electricity customers).

3.7. The internet is also having a noticeable effect on how consumers find out about deals before switching. While doorstep selling continues to be the most frequent method, switching because of doorstep selling has fallen in 2009. In contrast, switching through online comparison services has grown significantly. In 2009, 33% of gas customers found out about their last switch through door step sales (compared with 41% in 2008) and 26% via an online comparison site (compared with 21% in 2008). These percentage figures do not differ greatly between gas and electricity customers, but do vary between customer groups, for example:

- Only 9% of PPM customers switched using an online comparison site;
- Only 11% of those aged 65+ switched using an online comparison site (compared to 31% of those aged 15 -34).

3.8. On the proportion of gas customers who have ever switched, there is no change since 2008, where it remains at 43%. While the proportion of electricity customers who have ever switched is up two percentage points to 42%. This suggests that nearly all gas customers and most electricity customers switching in 2008 had already switched at least once before.

3.9. Regional differences show that the levels of switching have been significantly higher in England than in Scotland and Wales for electricity, and higher than in Wales for gas. Overall, of those who have ever switched either fuel, more than half have now switched more than once and one in four switchers have now switched three times or more.

3.10. Of those of who have never switched, the majority (83%) of customers on either fuel are aware that it is possible to switch, but this still leaves 1 in 5 customers who are unaware. This proportion is similar to the proportion in 2008 (80%) and suggests that suppliers could be doing more to inform their customers of switching possibilities. The proportion of customers who are aware that it is possible to switch is significantly lower amongst the younger population and minority ethnic groups.

3.11. Motivations for switching either fuel continue to be led by saving money, while seeking better service remains a lesser concern, although it is particularly mentioned by those with electricity prepayment meters. There is no evidence of much attraction from "greener" tariffs or fixed price deals as a reason to switch, though dual fuel packages are mentioned by 6% of gas and electricity customers.

3.12. Of those customers who switched to save money, 67% of those who switched electricity supplier and 64% of those who switched gas supplier believe they are now paying less as a result of their switch. This is a statistically significant improvement for electricity, where in 2008, 62% said they believed they were paying less than they would have without switching.

3.13. Finally, around three-quarters of switchers, 75% of those who switched electricity supplier and 72% of those who switched gas supplier, agree that they found it easy to decide which deal to switch to. Similarly 78% of those who switched their electricity supplier and 76% of those who switched their gas supplier agree that they fully understand the key features of the deal that they switched to.

## 4. Next Steps

4.1. This report has presented an update on how tariff differentials have changed over the period since Ofgem started its Probe investigation in October 2007 and, in particular, since the introduction of SLC 27.2A and 25A. We have also presented research on recent levels of switching activity. The analysis has shown that the licence conditions have been successful in delivering substantial reductions in the tariff differentials identified during the Probe.

4.2. However, the analysis in this paper shows that some individual areas of concern remain and some new issues have emerged, which require further consideration. In some cases, where we believe that there is a possibility that SLC 25A has been breached, we have already moved to Stage 1 of our bespoke enforcement procedure, as set out in the Guidelines published alongside the new conditions. We continue to monitor all areas of concern.

4.3. We are also monitoring the energy retail markets more widely and this report represents the first in a series of publications on developments. We intend each publication to focus on a different topic from the remedies package. Future topics may include, for example, further analysis of switching and consumer engagement, further evidence on suppliers' adherence to the Standards of Conduct, and trends in the micro-business market segment.

4.4. We are also committed to a thorough review of the impact of the measures introduced as a result of the Probe, before SLC 25A terminates at the end of July 2012.

## Appendices

### Index

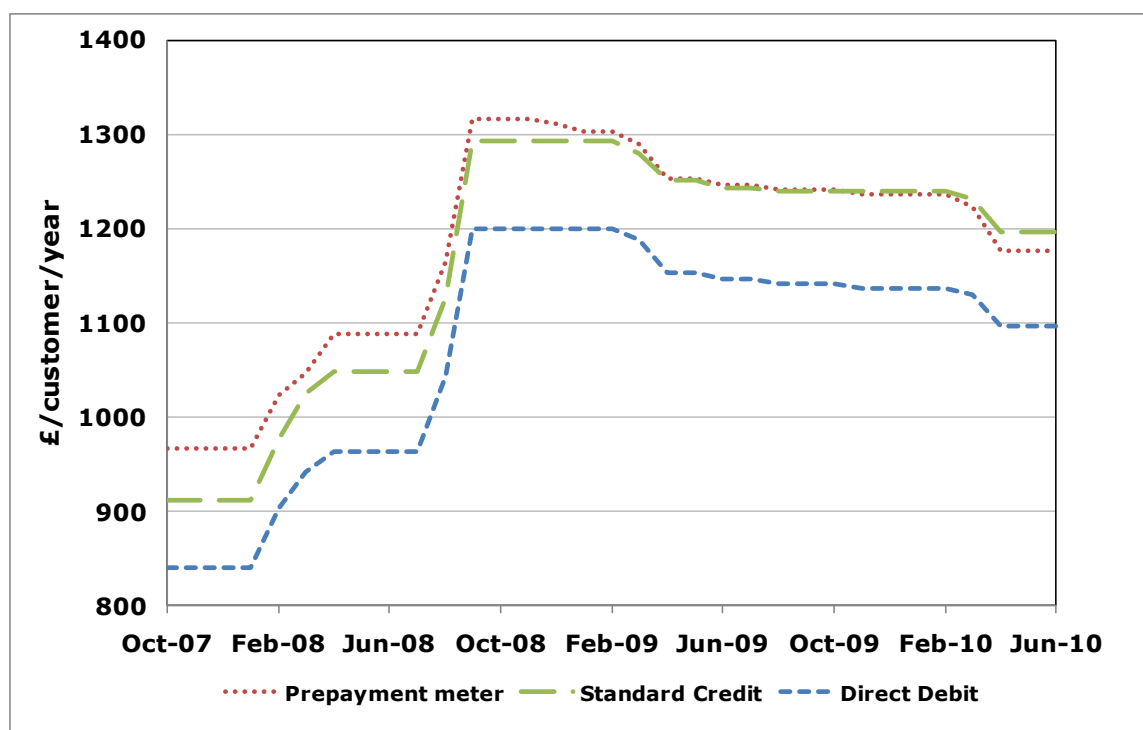
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## Appendix 1 – Average Annual Customer Bills

1.1. The analysis in chapter 2 of this paper focused on trends in tariff differentials within the domestic retail gas and electricity markets since October 2007. It focused on the GB market, as a whole, analysing how average tariff differentials between payment methods off-gas grid differentials, as well as the differentials on the tariffs charged by the five former electricity incumbents between “in-area” and “out-of-area” customers have moved over the past two years. This appendix provides some analysis looking at trends in total customer bills.

1.2. Figure A1.1 presents the average annual customer bill, across the Big 6, for a DD, SC, and PPM dual fuel bill as well the average across the three. The figure assumes constant annual electricity and gas consumption of 3.3MWh and 20.5MWh.

**Figure A1.1: Average annual dual fuel bills by payment method**



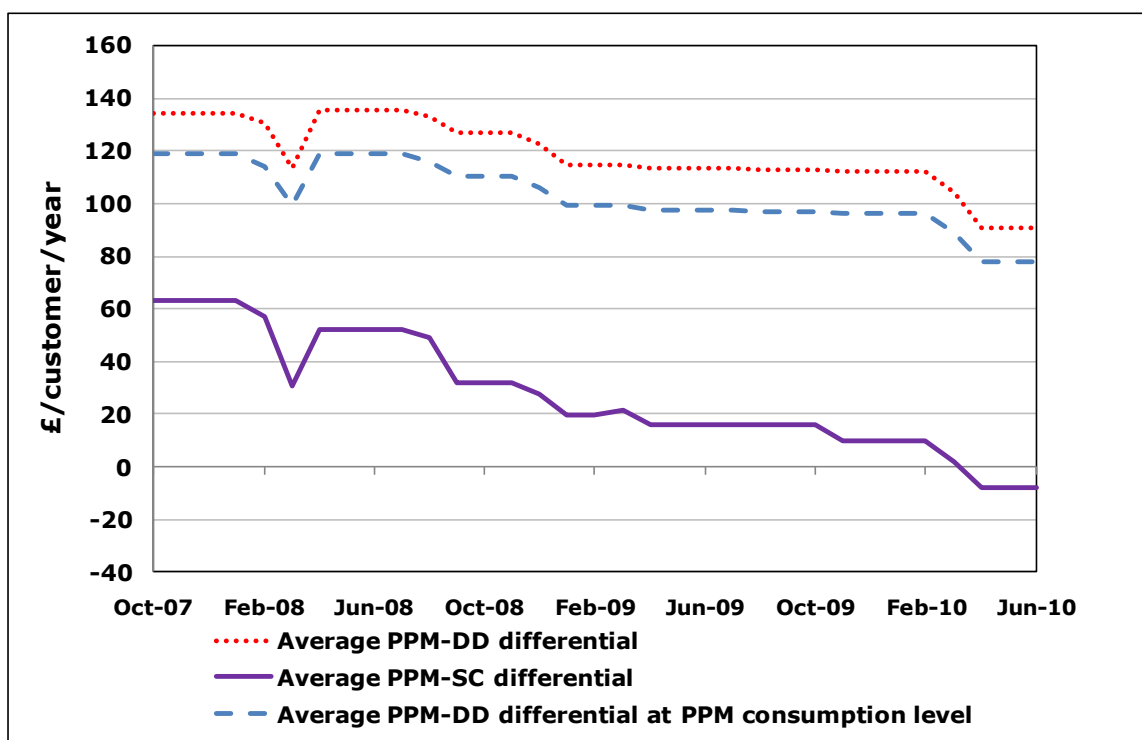
Source: Ofgem analysis

1.3. Figure A1.1 highlights the rise and fall in bills over the period presented. A significant driver of the increase in bills was related to the increase in wholesale energy costs during 2008. Since then, wholesale energy prices have fallen and during 2009, suppliers reduced retail energy bills. Figure A1.1 shows that during this time PPM tariffs fell faster than SC, resulting in an erosion of the average PPM-SC premium.

**Appendix 2 – Trends in Scotland and Wales**

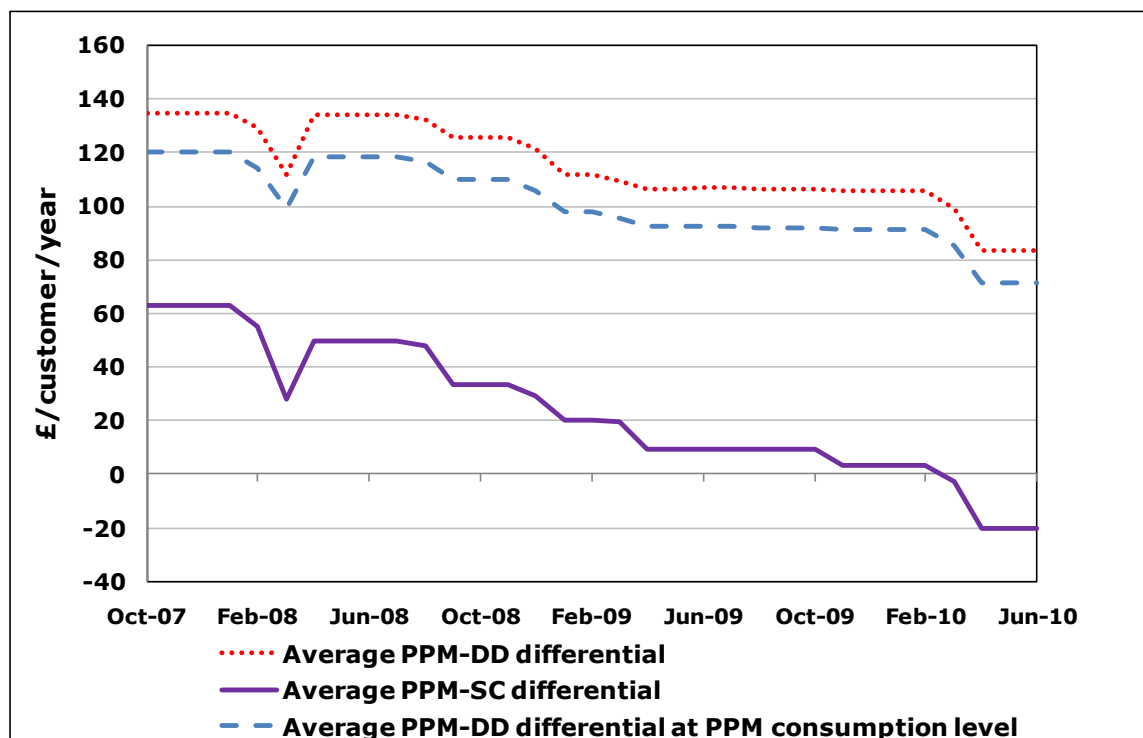
1.1. Figures A2.1 and A2.2 present the average PPM premiums in the Scottish and Welsh ex PES regions, respectively<sup>21</sup>. Figure A2.1, indicates that the Scottish PPM – DD premium, at average consumption, has fallen to £91 from a peak of £136, in the middle of 2009. Figure A2.2 shows that customers paying by prepayment meter in the Welsh ex PES regions pay £84 on average above customers paying by direct debit. Both these values are slightly above the GB equivalent value of £81.

**Figure A2.1 Average PPM premiums – Scottish PESs only**



Source: Ofgem analysis

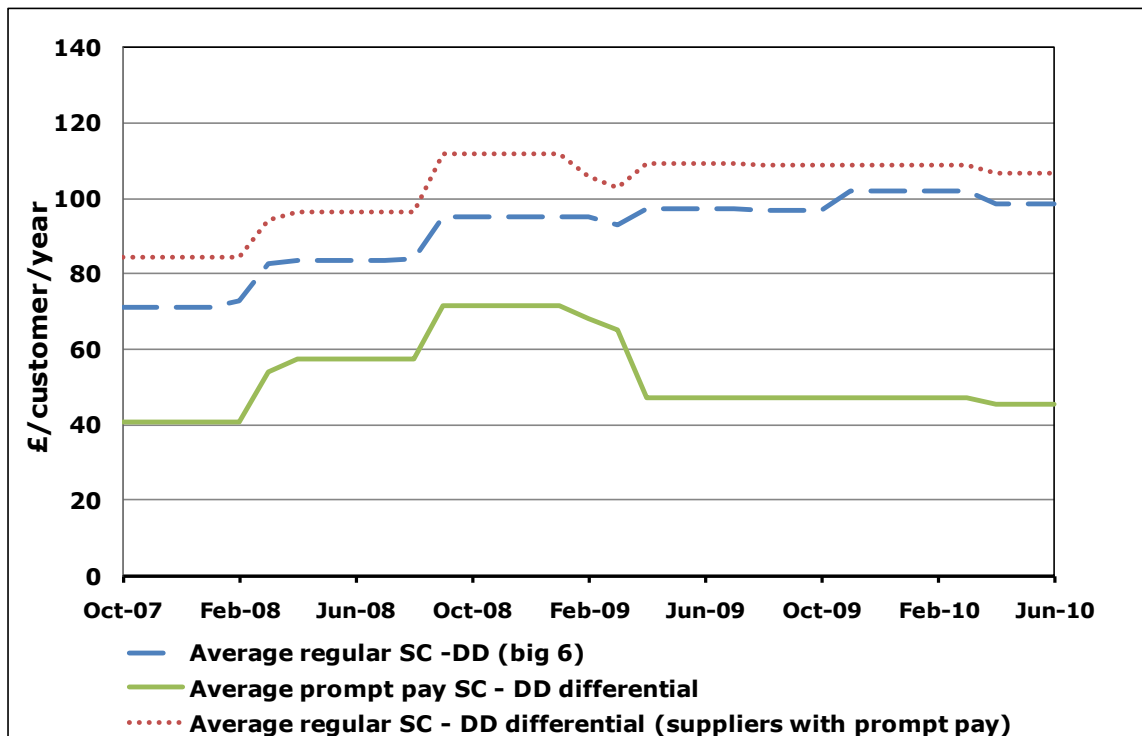
<sup>21</sup> Using Manweb and Swalec regions as a proxy for Wales, and Scottish Power and Scottish Hydro regions for Scotland

**Figure A2.2 Average PPM premiums – Welsh PESs only**

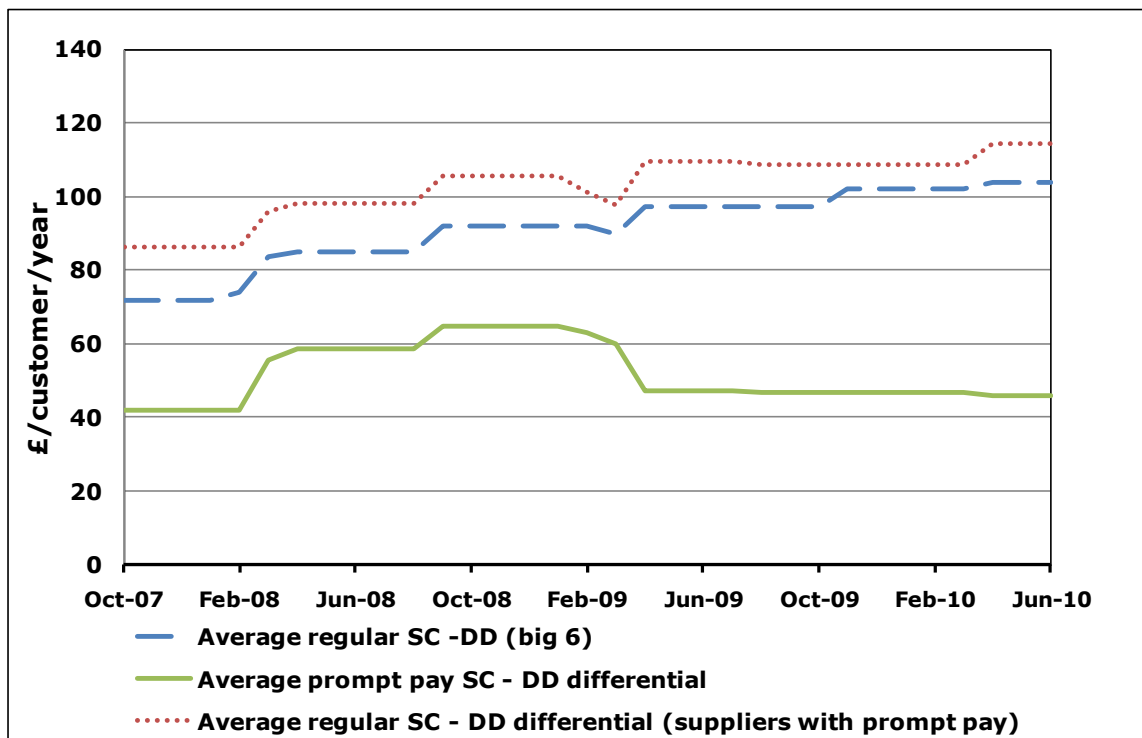
Source: Ofgem analysis

1.2. Figures A2.3 and A2.4 present the average SC premiums in the Scottish and Welsh ex PES regions, respectively. The charts are similar to that of the GB average. Both figures indicate that the SC – DD premium, for suppliers who offer prompt-pay, has increased to over £100 from just under £90, in October 2007. This compares with the current average SC – DD premium in GB at £109. Figures A2.3 and A2.4 also indicate that customers earning prompt pay discounts in Scotland and Wales can benefit to a similar degree as the average customer in GB.

**Figure A2.3 Average SC premiums – Scottish PESs only**



**Figure A2.4 Average SC premiums – Welsh PESs only**



Source: Ofgem analysis

1.3. Comparing in vs. out of area differentials for Scotland and Wales is very much affected by the individual pricing policies of the two original incumbent suppliers in each region. This is less of an issue for GB as a whole where there are 14 ex incumbents. However, we note that the average differential is currently (about £13) above the GB average in Scotland, and slightly (about £6) higher than the GB average in Wales, and while the overall trend in GB since we launched the Probe has been downward, it has been upward in Scotland and Wales. This means that customers paying by standard credit in Scotland, purchasing electricity from their incumbent supplier, are now paying around £30 more than customers who have switched to a different supplier, an increase of £16 since October 2008. This pattern is repeated in Wales, with customers purchasing electricity from their incumbent supplier paying around £23 more, representing an increase since October 2008 of £18.

1.4. It is important to stress the limitations of our methodology in reaching these results - a higher in-area premium for Scotland or Wales represents the difference between incumbent suppliers' charges in these regions, and non-incumbent suppliers' charges in the same regions. The premiums are therefore heavily affected by the charging behaviour of individual suppliers, and also reflect an amount that customers in these regions could save by switching.

## Appendix 3 – The Authority’s Powers and Duties

1.1. Ofgem is the Office of Gas and Electricity Markets which supports the Gas and Electricity Markets Authority (“the Authority”), the regulator of the gas and electricity industries in Great Britain. This appendix summarises the primary powers and duties of the Authority. It is not comprehensive and is not a substitute to reference to the relevant legal instruments (including, but not limited to, those referred to below).

1.2. The Authority’s powers and duties are largely provided for in statute (such as the Gas Act 1986, the Electricity Act 1989, the Utilities Act 2000, the Competition Act 1998, the Enterprise Act 2002 and the Energy Acts of 2004, 2008 and 2010) as well as arising from directly effective European Community legislation.

1.3. References to the Gas Act and the Electricity Act in this appendix are to Part 1 of those Acts.<sup>22</sup> Duties and functions relating to gas are set out in the Gas Act and those relating to electricity are set out in the Electricity Act. This appendix must be read accordingly.<sup>23</sup>

1.4. The Authority’s principal objective is to protect the interests of existing and future consumers in relation to gas conveyed through pipes and electricity conveyed by distribution or transmission systems. The interests of such consumers are their interests taken as a whole, including their interests in the reduction of greenhouse gases and in the security of the supply of gas and electricity to them.

1.5. The Authority is generally required to carry out its functions in the manner it considers is best calculated to further the principal objective, wherever appropriate by promoting effective competition between persons engaged in, or commercial activities connected with,

- the shipping, transportation or supply of gas conveyed through pipes;
- the generation, transmission, distribution or supply of electricity;
- the provision or use of electricity interconnectors.

1.6. Before deciding to carry out its functions in a particular manner with a view to promoting competition, the Authority will have to consider the extent to which the interests of consumers would be protected by that manner of carrying out those functions and whether there is any other manner (whether or not it would promote competition) in which the Authority could carry out those functions which would better protect those interests.

1.7. In performing these duties, the Authority must have regard to:

<sup>22</sup> Entitled “Gas Supply” and “Electricity Supply” respectively.

<sup>23</sup> However, in exercising a function under the Electricity Act the Authority may have regard to the interests of consumers in relation to gas conveyed through pipes and vice versa in the case of it exercising a function under the Gas Act.

- 
- the need to secure that, so far as it is economical to meet them, all reasonable demands in Great Britain for gas conveyed through pipes are met;
  - the need to secure that all reasonable demands for electricity are met;
  - the need to secure that licence holders are able to finance the activities which are the subject of obligations on them<sup>24</sup>; and
  - the need to contribute to the achievement of sustainable development.

In performing these duties, the Authority must have regard to the interests of individuals who are disabled or chronically sick, of pensionable age, with low incomes, or residing in rural areas.<sup>25</sup>

Subject to the above, the Authority is required to carry out the functions referred to in the manner which it considers is best calculated to:

- promote efficiency and economy on the part of those licensed<sup>26</sup> under the relevant Act and the efficient use of gas conveyed through pipes and electricity conveyed by distribution systems or transmission systems;
- protect the public from dangers arising from the conveyance of gas through pipes or the use of gas conveyed through pipes and from the generation, transmission, distribution or supply of electricity; and
- secure a diverse and viable long-term energy supply, and shall, in carrying out those functions, have regard to the effect on the environment.

1.8. In carrying out these functions the Authority must also have regard to:

- the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed and any other principles that appear to it to represent the best regulatory practice; and
- certain statutory guidance on social and environmental matters issued by the Secretary of State.

1.9. The Authority may, in carrying out a function under the Gas Act and the Electricity Act, have regard to any interests of consumers in relation to communications services and electronic communications apparatus or to water or sewerage services (within the meaning of the Water Industry Act 1991), which are affected by the carrying out of that function.

1.10. The Authority has powers under the Competition Act to investigate suspected anti-competitive activity and take action for breaches of the prohibitions in the legislation in respect of the gas and electricity sectors in Great Britain and is a designated National Competition Authority under the EC Modernisation Regulation<sup>27</sup> and therefore part of the European Competition Network. The Authority also has

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<sup>24</sup> Under the Gas Act and the Utilities Act, in the case of Gas Act functions, or the Electricity Act, the Utilities Act and certain parts of the Energy Acts in the case of Electricity Act functions.

<sup>25</sup> The Authority may have regard to other descriptions of consumers.

<sup>26</sup> Or persons authorised by exemptions to carry on any activity.

<sup>27</sup> Council Regulation (EC) 1/2003.

concurrent powers with the Office of Fair Trading in respect of market investigation references to the Competition Commission.

## Appendix 4 – Feedback Questionnaire

1.1. We are keen to consider any comments or complaints. In particular, we would be keen to get your answers to the following questions:

- Does the report adequately reflect your views? If not, why not?
- Does the report offer a clear explanation as to why not all the views offered had been taken forward?
- Do you have any comments about the overall tone and content of the report?
- Was the report easy to read and understand, could it have been better written?
- Please add any further comments?

1.2. Please send your comments to:

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Consultation Co-ordinator  
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